



July 21, 2016

Ms. Sarah Rees
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Mr. Stuart Clark
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Washington State Department of Ecology
PO Box 47600
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RE: Formal Comments regarding the Washington Clean Air Rule

Dear Ms. Rees and Mr. Clark:

Thank you for providing us the opportunity to submit comments on the revised draft of the Washington State Department of Ecology Clean Air Rule that aims to cap global warming pollution in Washington State. These comments are submitted on behalf of Climate Solutions, Natural Resources Defense Council, NextGen Climate, Sierra Club, Union of Concerned Scientists, and Washington Environmental Council.

We commend Governor Jay Inslee for responding to legislative inaction and implementing Washington's Clean Air law by pursuing rulemaking to reduce Washington State's carbon pollution to protect current and future generations from the impacts of climate change and air pollution. Comprehensive, well-crafted action on climate will help transform Washington's economy into one that is more sustainable and equitable. It is imperative to pursue a bold policy that takes full advantage of authority that exists under the Clean Air Act and in judicial orders requiring the State to act on carbon emissions, though we recognize that the policy options offered through this path are more limited than those available with legislative cooperation or through an initiative to develop an economy-wide carbon policy.

SUMMARY

We acknowledge and appreciate the changes the Department has made to the previously released draft rule, including the addition of a reserve account, a registry, and initial steps toward an aggregate cap over all covered sectors of the economy. These changes have made this a stronger rule than the draft originally released. However, more work is required to strengthen the rule's ability to reduce carbon emissions and to better clarify its implementation. We remain deeply concerned that the proposed Clean Air Rule is insufficient as a means to achieve the state's carbon reduction goals and sets a concerning precedent for other jurisdictions to follow. The summary of our comments is as follows:

A. Program Architecture

As shared in [previous comments](#) and forums, the baseline-and-credit system is a flawed approach to regulating carbon emissions. Switching the Clean Air Rule to an aggregate cap with distribution of a limited and declining pool of allowances would reduce accounting and verification requirements, ensure integrity of reported emissions reductions, ensure liquidity of tradable compliance instruments, create

better opportunities for linkage with other markets (including those potentially created by the Clean Power Plan), and create a pathway to avoiding windfall profits, while reducing the extreme reliance on offsets as the primary compliance method and reducing the administrative burdens on State agencies. If the Department does not make this important change to the architecture of the Clean Air Rule, then it should pre-certify ERUs from on-site reductions ahead of the 3-year compliance deadline.

B. Aggregate Cap

While we appreciate that the Department took initial steps towards creating an implicit aggregate cap on economy-wide emissions, we do not believe that the Clean Air Rule goes far enough in articulating the overall limit. The rule should set an explicit and declining cap for carbon emissions and ensure that aggregate emissions from all regulated entities never exceed that limit. We also urge the Department to consider a more ambitious compliance pathway consistent with best available science.

C. Offsets

As a result of the rule's baseline-and-credit structure, the draft rule depends on emission reduction projects or programs, otherwise known as offset projects. Offsets, or projects to reduce emissions that do not directly result in emissions reductions at the regulated facilities, will likely be the primary means of compliance for some if not all sectors. This is an unprecedented approach that will cause a significant and ongoing verification and tracking burden on Ecology and could limit the impact of the rule. Furthermore, the fact that offsets can include projects within the regulated sectors raises significant issues of double counting and additionality that may cause the Clean Air Rule to fail to achieve real reductions consistent with state-mandated goals.

D. Reserve Account

The addition of the reserve was a key recommendation of the environmental community. While we appreciate that the updated draft incorporates this concept, we believe more work needs to be done to properly structure this account, including ensuring sufficient deposits, how credits are allocated to the account, and other considerations that we address in our detailed comments below.

E. Curtailment

Provisions to address curtailment of production from covered sources were other substantial issues with the first version of the Clean Air Rule. While the draft rule's new provisions are a step in the right direction, a number of significant loopholes remain as noted below.

F. Voluntary Participants

The inclusion of voluntary participants, as currently structured, does not meet the requirement of additionality in crediting emissions reductions. Voluntary participants that are not subject to ongoing reductions requirements and can leave the program at will, will likely be rewarded for business as usual activities, reducing emission reduction obligations for other facilities.

G. Electricity Sector Exemption for CPP Compliance

Because of other design decisions and statutory limitations, the Clean Air Rule will not be eligible as a compliance plan for the federal Clean Power Plan. However, Ecology should require that when the utility sector regulation shifts to the Clean Power Plan, its reduction pathway remains at least as ambitious as proposed in this rule and preferably is consistent with best available science.

H. Biofuels

Because of limitations on the use of lifecycle analysis in evaluating the carbon content of fuels, the Clean Air Rule does not accurately account for the greenhouse gas benefit of using biofuels versus fossil fuels. To address this shortfall, it would be preferable to follow the approach used by California to exempt the

carbon emissions associated with biofuels and work towards a more comprehensive assessment of the carbon attributes. This is also consistent with the biomass exemption currently in the rule.

I. Additional Recommendations

We provide additional recommendations to immediately incorporate EITE businesses into the reduction requirements and to ensure that the rule does not inadvertently lead to increased pollution that harms air- and water-quality, particularly in communities already impacted by contaminants.

RECOMMENDATIONS & CLARIFICATIONS

A. Program architecture

We remain very concerned with the decision to pursue a baseline-and-credit approach instead of the simpler, tested and well-understood economy wide cap. Fundamentally, a baseline-and-credit structure limits the creation of a transparent and liquid market that reduces costs through efficient distribution of emissions reductions while ensuring the state meets its emissions reductions target.

A summary of these concerns is included below. Please also find attached other memos we have previously shared for more detailed discussions of these issues and which we incorporate into these comments.

Liquidity concerns

An economy-wide cap requires a functioning trading system to address the varying costs of compliance at each regulated facility. This flexibility is important to reduce leakage risk for jobs and emissions—creating on-paper reductions that are merely replaced with pollution elsewhere. An allowance system—which provides legally verified emissions permits at the outset—allows companies to trade based on their projected need, provides incentives for early on-site reductions, and offers companies a compliance flexibility option that preserves the integrity of the pollution cap.

Because tradable emission reduction units (ERUs) are only issued following a compliance determination there will be significant uncertainty in market-wide availability and demand for ERUs. This will lead to boom and bust cycles—high demand prior to a compliance determination with low numbers of certified ERUs, followed by the issuance of credits with little immediate demand for them.

The baseline-and-credit design choice also undermines a core function of emissions trading—providing a financial reward for early movers that helps finance pollution-reduction projects. While a facility in an allowance system would be able to generate market revenue from emissions reductions immediately, under the proposed Clean Air Rule, the same facility would be unable to recoup costs for as much as three and a half years and would be unable to predict the revenue it can expect from trading. The result is that facilities will be incentivized to *avoid* on-site reduction projects, preferring instead the certainty of offsets. Fenceline communities, which would most immediately benefit from such projects, will instead see pollution mitigation funding leave their community and get spent elsewhere.

Linkage

A baseline-and-credit approach significantly limits the ability of the Washington Clean Air Rule market to link with external trading systems, such as the Western Climate Initiative (WCI), and is not compatible with the Clean Power Plan. This architecture is fundamentally incompatible with economy wide or sectoral emissions caps, exemplified by the Department of Ecology's proposed one-way linkage with California's emissions trading market and lack of connection with EPA's 111d rule. California allows any entity to purchase and retire allowances, and thus will likely not preclude Washington from allowing

regulated entities to do so for compliance, but California would not allow purchase of Washington ERUs for compliance in their program. Use of California allowances will likely only act as effective price cap for the WA program; i.e., in-state entities would likely only purchase California allowances if they were unable to purchase lower cost ERUs or offsets elsewhere.

Likewise, this architecture eliminates any possibility of creating a rule that coherently integrates with the Clean Power Plan. Instead of creating an avenue for a state measures approach, as California is pursuing, the Clean Air Rule proposes to regulate Washington's in-state power sector initially under the rule before shifting regulation to the Clean Power Plan. This inconsistency will make alignment with the Clean Power Plan more difficult and will mean that after the power sector phases out of the Clean Air Rule, there is an even smaller number of regulated facilities and an even less transparent and liquid ERU market.

Windfall Profits

The baseline and credit approach is identical to a free allocation of allowances under an economy wide cap in one respect: regulated entities are likely to attribute the market cost of carbon to all emissions. While we doubt the UTC would allow regulated utilities to pass these opportunity costs onto customers, other industries are likely to do so, and to pocket the resulting windfall profits. This is one of the reasons other jurisdictions, including California and RGGI, have auctioned allowances or conditioned any free allocation on output-based updating.

Recommendations

The Department has the opportunity to use a proven, straightforward, and legally sound approach but has instead chosen a path that is more uncertain, complicated, and likely fraught with error. We strongly urge the Department to replace the Clean Air Rule's baseline-and-credit structure with an allowance approach. Doing so would enable the state to benefit from learned experience from WCI, the European Union's Emission Trading System, RGGI, and a variety of non-carbon cap-and-trade systems.

If the Department does not make this important change to the architecture of the Clean Air Rule, then it should pre-certify ERUs from on-site reductions ahead of the 3-year compliance deadline. For example, should an industrial facility achieve significant on-site reductions following an efficiency upgrade, the facility could generate pre-certified ERUs that will be available for immediate sale to parties needing compliance instruments to meet their own reduction obligations. Doing so would increase the supply of non-offset ERUs between compliance periods, provide earlier financial reward for companies investing on-site and marginally increase liquidity for all covered facilities. However, we strongly maintain that there is *no substitute* for this significant fix to the architecture.

B. Aggregate cap

Explicit emissions limit

In addition to calling for an architectural overhaul, one of the principal requests of the environmental community following the initial draft rule release was the addition of an aggregate cap. This cap would provide greater clarity on emission trajectory and an overall limit for economy-wide pollution. With the benefit of this cap, the Department would be able to structure and properly allocate baselines to covered entities in a way that facilitates steady reductions and accommodates new entrants. A number of recommendations in this comment letter, including options for charging the reserve account, depend on an upfront declaration of overall reduction requirements.

While we appreciate that the Department added an implicit cap to this new draft rule (referenced in WAC 173-442-020 (1)(r) & (2)) by creating a set-aside from compliance pathways to allow for new entrants, the proposed rule still lacks an explicit statement of total reductions required.

Ambition of Emissions Reduction Goals

In 2009 Governor Gregoire issued an executive order, finding in part that “greenhouse gases are air contaminants within the meaning of the state’s Clean Air Act and pose a serious threat to the health and welfare of Washington’s citizens and the quality of the environment.” This finding follows the endangerment finding by US EPA that was affirmed by the US Supreme Court. These findings obligate the EPA and Washington’s Department of Ecology to regulate carbon emissions and, in doing so, to consider limits necessary to achieve protection of the global atmosphere in accordance with the best available science. The current rule adopts targets based only on the statutory goals for emissions reductions in Washington law in RCW 70.235.020. That section does not preclude deeper emissions cuts—since a more ambitious program would also achieve the minimum reductions codified in that section, it only precludes a less ambitious program.

Furthermore, we recommend that Ecology regularly review the effectiveness of the established emission reduction pathways. The rule should include the flexibility to adjust the caps as appropriate to ensure the reductions are aligned with state, national and international objectives for emission reductions. Several carbon markets have lowered their caps to more accurately account for the introduction of low cost emission reduction options and changing market conditions. Regular review of the program’s stringency at scheduled times will help to ensure that Washington’s emission caps continue to drive improvements over business as usual while providing businesses with the expectation to plan for future changes to the caps.

Recommendations

We believe that the Department should embrace the broadest interpretation of its authority under the Clean Air Act and [judicial rulings](#) in the King County Superior Court with regard to the Our Children’s Trust lawsuit. While we strongly support the Department submitting new emissions recommendations to the legislature, this rule is fundamentally a response to the legislature’s inaction in the face of crisis. Given this simple fact, the Department of Ecology should embrace its authority now, instead of waiting for further legislative action, by articulating an explicit cap and pursuing the emissions reduction trajectory that the scientific consensus demands.

C. Offsets

The baseline-and-credit system’s significant limitations led the Department to create artificial liquidity within the Clean Air Rule emissions market through the nearly unrestricted use of offsets, both in terms of quantity and type. This sets a deeply troubling precedent by allowing companies to buy their way out of compliance without making meaningful on-site reductions, while at the same time building in a massive risk of double-counting that will further reduce the accountability that a carbon cap system is intended to create. These fundamental flaws in the rule’s design must be addressed.

High proportion of allowed offsets

Offsets are intended to provide an external source of emissions reductions for facilities that cannot otherwise economically or logistically comply with a cap. Flexibility within trading systems is important to prevent leakage of jobs and emissions to areas with laxer standards, but the Clean Air Rule’s intention to allow offsets to serve 100% of compliance obligations (WAC 173-442-100) would be unprecedented among successful carbon cap regimes. Allowing this high level of offsets compliance seems to imply that

facilities have no ability to comply through improvements in efficiency, increased use of clean energy or reduction in fuel consumption within the covered sectors.

Reaching our state's climate goals will entail serious improvements at facilities themselves and within the regulated sectors. These investments and efficiencies in renewable fuels and clean energy will support local jobs and lead to critical air quality improvements for fence-line communities, which usually are communities of color and low-income communities that are most directly impacted by our economy's overwhelming dependence on health-compromising fossil fuels. Unfortunately, relying so heavily on offsets means it's likely that many of these benefits will not be realized.

Additionally, the reduction trajectories outlined under this rule only cover the portion of Washington State emissions for which covered entities are responsible, implying that additional policies and reductions will be required to address the reduction of uncovered emissions. However, the broad use of offsets in the CAR likely means that the easiest and least costly emissions reductions from *all* sources will likely be used to meet the compliance obligation of the covered CAR entities. While we might expect a rule like this to lead to reductions within the 60% of the economy it covers, with provision for a small fraction of reductions to come from outside in the form of offsets, while complimentary policies help the other 40% achieve pollution reductions, the Clean Air Rule will actually generate reductions from low-hanging fruit throughout the state. This delays but does not eliminate the need to reduce within covered sectors.

Double-counting risk

Emission reduction projects that are generated from within a regulated sector will, if successful, result in emission reductions while also generating a subsequent ERU. For example, a company investing in a truck stop electrification project will contribute to reduced diesel demand from long-haul vehicles that would normally idle overnight. The investor receives an ERU; and the reduced diesel usage will mean reduced diesel imports or refinement that will mean lower compliance obligations at oil refineries and importers —each one-ton reduction will thus be counted twice. Reduction of diesel usage is a laudable goal, but it should certainly not be double-counted within the Clean Air Rule market. This defect applies to other covered sectors and is present throughout the rule. As detailed in Renewable Northwest's comments, double-counting would also have negative impacts on Washington's existing clean energy policies, such as the Renewable Portfolio Standard and the voluntary renewable energy market.

Moreover, double-counting means that even as facilities file on-paper reductions that appear to comply with the Clean Air Rule, actual reductions may be substantially lower.

While we appreciate the rule's inclusion of an intent to retire ERUs from the reserve for offsets generated within the capped sectors, we are still wary that 1) significant resources will be required for sufficient tracking and verification to accurately account for the impacts of emissions reduction projects and 2) whether there will be a sufficient quantity of ERUs in the reserve available to be retired to eliminate double counting (see below).

Definition of "additionality"

In articulating the criteria for an acceptable offset ERU in the program, the rule states that a reduction must be "additional to existing law or rule" (WAC 173-442-150 (1)(e)). First, without addressing double-counting, onsite emissions reductions (or ERUs created as a result of a facility exceeding its baseline) that occur as a result of renewable energy used for I-937 compliance or the voluntary renewable energy market would not meet the definition of additionality. Second, this limited definition is out of step with broadly accepted principles of carbon reduction—a carbon reduction that would not exist but for this rule. Facilities may undertake reduction projects for many reasons beyond regulation, most especially

because doing so is cost effective over the life of the project. Crediting of offset ERUs should be limited only to projects that the Clean Air Rule is directly and solely responsible for, a key safeguard for ensuring new investments. We recommend expanding the definition of additionality to also include reductions that “exceed any greenhouse gas reductions that would otherwise occur in a conservative business-as-usual scenario.” This definition is consistent with the Western Climate Initiative design criteria and California’s cap-and-trade program’s definition of additionality.

In particular, and as discussed later in the letter, this correct application of the additionality principle is violated by the Clean Air Rule’s method of allowing voluntary entrants into the market.

Ecology-approved additional offset protocols

The Department has also reserved the power to approve additional, new offset protocols for a variety of different types of projects—combined heat and power explicitly, but also new approaches for all listed reduction activities (WAC 173-442-160 (10)). Because this rule will likely be administered with limited resources, it may be difficult for the Department to undertake the significant research and analysis necessary to truly understand if the new proposals are indeed real, permanent, enforceable, verifiable and, crucially, additional.

The rule also does not articulate any process for transparency or public input into the determination process. Given existing concerns with definitions and approach to offsets, we worry that this will lead to approval of new offset protocols that will not meet stringent requirements. Especially coupled with the issues raised above, this sets a problematic precedent.

Recommendations

A broad range of improvements and fixes are necessary to limit the significant potential for offset abuse in the current proposal. The simplest and most rigorous solution for these problems is to allow only dependable, existing protocols in the program and eliminate all regulated-sector offset opportunities. While the prospect of retiring ERUs from the reserve account to mitigate the effect of double-counting may help to partially alleviate the effects of this shortcoming, it is not likely to be sufficient. On the other hand, by allowing only a limited number of offsets from non-regulated facilities like agriculture and out-of-state projects that also meet additionality requirements through well understood and documented protocols, the rule can restore integrity to the cap and provide greater confidence that when offsets are used they are indeed additional to business as usual.

Furthermore, the Clean Air Rule should restrict reliance on offsets by allowing them to fulfill only a portion of total compliance obligation. Similar to the offset restrictions in California’s cap-and-trade program, this would reduce the need for such widespread use of in-sector instruments while compelling greater facility investment. We understand that Ecology chose to restrict the role of out-of-state compliance instruments to ensure that pollution reduction projects benefited Washington residents, a high-level goal we share. But doing so merely leads to reduced aggregate reductions through double-counting. It would be highly preferable to reduce the role and types of offsets while lifting restrictions on their geographic origin—thereby ensuring that any protocol used will ensure real and additional reductions while guaranteeing that Washington communities benefit from in-state reductions.

To the extent that the Department does approve new protocols, it is important that the rule identify a rigorous process with opportunities for public input to verify that offsets meet strict standards of emission reductions.

Additional recommendations for correcting potential issues related to emission-reducing activities or programs are outlined in Section 7 of the comments submitted by Stockholm Environment Institute (SEI) on June 28, 2016.

D. Reserve Account

The addition of a reserve account to the Clean Air Rule market is a substantial improvement over the previous rule draft. The account provides a mechanism for preserving the overall integrity of the emissions cap while creating space for new market entrants and addressing the risk of double-counting. While we believe the reserve account may help alleviate a number of concerns with the current structure of the Clean Air Rule, we are concerned that more work and clarification is needed to ensure that these goals are achievable.

Insufficient Charging Rate

While the addition of a supplementary compliance obligation to charge the reserve account on an ongoing basis is an appropriate way to distribute to all covered facilities the responsibility of creating room for new entrants and mitigate double-counting, the proposed amount for the charge is insufficient. In proposing the reserve account as a remedy for market entrances and exits, [SEI's February 12, 2016](#) memo, recommended a set-aside of 3.5% of the *total market emissions*, an amount totaling approximately 750,000 tons annually and climbing to about 1,000,000 in the second compliance period. This amount is roughly consistent with the reserve design in California and the RGGI program, both of which arguably have fewer built in demands on the reserve than in this proposal. In the proposed rule, the Department has instead chosen to allocate 2% of *compliance obligation* to the account (WAC 173-442-240 (1)(a)(i)(A)) or about 17,211 tons in the first year. This rate will create a disproportionate reliance on curtailments to fill the reserve, which as we discuss below, will create other problems.

Comparing the expected initial deposits to just one of the account's intended purposes—facilitating new entrants - reveals the insufficiency of the current charging level. In the first compliance year, 2% of compliance obligation totals approximately 17,211 tons, climbing in the following years. At this rate, a single mid-sized new facility emitting 300,000 tons would require the total aggregate deposits for the first six years of the program to be fully covered. A larger facility would take even longer. This does not take into account the account's other important purposes—double-counting mitigation, Environmental Justice Advisory Committee (EJAC) allocations, and the voluntary renewable energy market.

Charging Mechanism

Beyond the charging rate, we are also concerned about the charging mechanism, which depends on setting aside a certain amount of facilities' compliance obligations. In the event that all or most facilities comply with offsets (a likely outcome in the proposed baseline-and-credit system), there is a substantial risk that the reserve account is never fully charged—each deposited offset from within the covered sector would need to be compensated with a retired ERU already in the account to eliminate double-counting.

Prioritization

While we understand the many goals assigned to the Reserve Account, we are concerned by the prioritization of goals (WAC 173-442-240 (4)), which implies that not all of them will be served. Of the first five goals listed for the account, failure to meet any one of them would mean that the state falls short on the Clean Air Rule goals and the emissions reductions required by statute. It would be unacceptable, for example, to accommodate new entrants while allowing widespread double-counting of emissions reductions, an outcome permitted by the current prioritization in the rule. While this would

result in addressing the impact of a new facility, the over-crediting of emissions reductions means that what looks like a reduction toward statutory goals is not actually realized.

Providing space for new and restarting entrants, double-counting mitigation, environmental justice support, and maintaining the integrity of the voluntary renewable energy market are all important goals for the Clean Air Rule to strive for and should not be prioritized. Instead the reserve account should be structured to enable it to serve each goal.

Fungibility of ERU sources

In the current proposal, ERU sources are not differentiated based on how each credit is generated—a reserve ERU deposited as a result of curtailment is treated equally to one deposited as a result of on-site pollution reduction at a compliance facility. This ignores the nature of curtailment and leakage. Treating every ERU source fungibly assumes that each one is real and additional, but curtailment reductions generally do not meet this test. A facility that shuts down in Washington will likely see its production replaced outside of the state, leading to an emissions increase elsewhere that offsets a significant fraction of the Washington reduction.

While this kind of leakage must be avoided, in the case that it does happen, these credits should be only applied to other reserve account purposes sparingly and carefully. Because of their limitations, these reductions should only be used to counteract growth in Washington that is likely causing emissions reductions elsewhere. Setting aside curtailment ERUs for the purposes of production restart or new market entrants—which would likely lead to a production reduction elsewhere—would be an acceptable way to apply these credits. Curtailment ERUs should not be used, for example, to mitigate for double-counting where the Department should retire a real emissions credit to preserve the integrity of the cap.

Over-counting of reductions from EJAC projects

We share the desire to invest in key environmental justice priorities to reduce the impact of fossil fuel combustion on vulnerable communities adjacent to facilities and mobile sources of pollution. As such it is important that the program maximize the opportunities to reduce emission of co-pollutants of fossil fuel combustion, such as criteria and toxic pollution, in vulnerable communities. We believe that the hybrid mechanism of offsets and ERU allocation could undermine these objectives and weakens the integrity of the cap (WAC 173-442-240 (3)(b)(iv)). Projects receiving ERUs will themselves generate emission reductions, leading to at a minimum double-counting of credits. If, as the rule suggests, ERUs are rewarded at a rate that is greater than one to one, it is possible instead of promoting improved public health outcomes in these neighborhoods, the EJAC allocations will lead to an even steeper level of over-crediting that will guarantee that the Clean Air Rule fails to achieve its stated objectives.

Limited definition of double-counting

The rule defines double-counting as a situation where more than one ERU is generated for an emission reduction project (WAC 173-442-240 (2)(b)) . While addressing this is important, not all emissions reductions will yield an ERU. In cases where the second credited emission reduction helps a facility reach its baseline (as opposed to exceeding it), no ERU credit is generated, but double-counting has still occurred. Double-counting mitigation should address this concern as well. This concern is addressed at more length in Section 2 of SEI's comments submitted June 28, 2016.

Recommendations

We urge the Department to pursue the original recommendation in SEI's February 12, 2016 memo, which we have previously endorsed. Charging the account should be achieved by creating an initial set-aside of the total aggregate emissions level, preferably 3.5% of the total. The remaining unallocated

emissions can be subdivided and assigned to each entity required to comply with the rule. It would be preferable to then eliminate entirely facility-directed regulated-sector offset selection and instead allow the EJAC and the Department to allocate the full complement of reserve ERUs to selected projects. This will generate a higher level of investment in targeted projects, provide a degree of needed flexibility to complying facilities, and simplify the mechanism for double-counting mitigation. This ensures that the reserve account is fully charged with actual ERUs that are not double-counted.

In the event that the Department chooses not to follow this preferred pathway, we recommend adding a variable reserve charge to each compliance facility to ensure that the account has a steady and sufficient stream of ERU deposits. This can be achieved by allowing the reserve account to go into deficit following a compliance period if demand for its ERUs is greater than the supply. The Department would then increase the reserve charge evenly for all compliance facilities to a level necessary to bring the account into balance. While a less than ideal solution, this mechanism would contribute to restoring the integrity of the cap and lead to steadily increasing investments in clean energy and pollution mitigation projects.

E. Curtailment

We strongly support a mechanism to prevent windfall profits that reward companies for shifting production outside of Washington. This kind of incentive contributes to substantial risk of job loss and emissions leakage. While the introduction of curtailment protections in this draft rule is a welcome step, we believe that the definition used is too narrow and the exclusion is too broad to fully protect Washington workers and the environment from abuse.

Definition too narrow

The included curtailment definition (WAC 173-442-020 (1)(k)) includes three major loophole categories that may benefit companies but harm workers and affect overall emissions reductions. These loopholes—exemptions for production stoppage of less than four months, reduction in production rate, and facility investments—would allow facilities to retain their baseline and in some cases generate ERUs nonetheless.

For example, under the current proposal, a facility that shutters production for three months does not meet the definition of curtailment. This kind of shut-down would lead to a 25% reduction in annual emissions levels at that facility, generating substantial ERUs that could be sold into the market to decrease others' reduction obligations. A company with facilities in multiple states would thus be able to shift production out of state for that time period, costing jobs and productivity in Washington, resulting in emissions leakage that would increase total emissions compared to the rule's goal. Slowing rates while shifting production would lead to the same outcome.

Similarly, other exemptions from the curtailment definition could lead to the same result. Exemptions for capital improvements and facility maintenance may not lead to the same negative job impacts in state, but would ultimately reduce the ability of the rule to actually achieve reductions consistent with the statutory emissions goals.

Remedy too broad

For those facilities that do curtail, the emissions reduction pathway is eliminated for the relevant years (WAC 173-442-060 (1)(b)(ii)). While under the current system, curtailment should exclude the facility's emissions from eligibility in participation in the market. To continue the state on its path toward reaching final reduction goals, it is important that upon restarting production-covered entities continue on track with the preset reduction curve.

Power sector exclusion

The power sector is entirely excluded from the curtailment definition (WAC 173-442-020 (1)(k)(ii)). While in-state power plants will regularly meet the definition as a result of variability in the hydropower system, this blanket approach creates significant risk of gamesmanship. Because the Clean Air Rule does not cover out-of-state power generation, the current proposal would generate new revenue for utilities that shift generation to non-Washington (potentially higher emitting and more costly) resources—generating ERUs that will be used to allow others to comply without changing behavior. As before, the total emissions picture is therefore unchanged while creating the appearance of pollution reduction.

Recommendations

To address risks of windfall profits from market exits and production reductions, we urge the Department to consider expanding the EITE output-based mechanism to all covered facilities. Doing so would accommodate changes of production without providing unfair advantage or creating incentives to shift jobs and emissions out-of-state. An output-based allocation of emissions reductions obligations would create space for both business cycle reductions and capital investments pauses in all years, including those subject to curtailment, while also accommodating economic expansion.

In the event that the Department chooses not to pursue an output-based allocation economy-wide or for the power sector specifically, we recommend adding an additional definition of "market exit" for electric generating units. While not fully addressing the issue of incentivizing leakage, applying curtailment policies once an EGU is inactive for some extended time period, for example six consecutive months, would reduce this risk.

F. Voluntary Participants

While we recognize that some entities that are not covered by the program would like to contribute to the effort to cut emissions and participate voluntarily, care must be taken that this voluntary participation actually contributes to additional emission reductions beyond BAU. Allowing for voluntary participation under the rule, as currently structured, opens up the potential for facilities under the compliance threshold to profit from business-as-usual while reducing the compliance obligation for other covered facilities. With the current structure of the program, a voluntary participant may have little incentive to opt in to the market unless they were already planning an emissions reduction project or production reduction. Allowing such companies to generate credits through BAU actions that are then sold into the market, therefore, will not generate new reductions or ensure that voluntary participants help reduce total economy-wide reductions.

The proposed rule does not require voluntary participants to achieve emission reductions beyond the level at which they enter the program (WAC 173-442-030 (6)(a)). They are also allowed to *exit* the program at will. This means that any business decision to generate ERUs will yield revenue for the participant, including reducing production in ways consistent with loopholes outlined in the curtailment section. In this way, small facilities can opt in to the market, generate revenue for a project or production slow-down, and opt out again to increase their emissions. All such actions will, at best, reduce pollution reduction in the state and, at worst, facilitate a higher level of emissions compared to Clean Air Rule goals.

Recommendations

Voluntary participation in the proposed program should only be allowed if the deficiencies outlined are addressed because, as currently laid out in the rule, it would be extremely difficult to ascertain the additionality of their production changes. To the extent that the rule does allow for voluntary

participation, it should include a process for establishing whether reductions are truly additional to business-as-usual and participants must be restricted in their ability to exit the program at will to ensure that their reductions aren't subject to backsliding that compromise cap integrity. Voluntary participants should also be given an emissions reduction requirement and generate ERUs beyond their stated goals in order to ensure that they are contributing to market-wide reduction goals. Section 8 of SEI's June 28, 2016 comments provides more details for addressing concerns with voluntary participation.

Current economic circumstances may lead to the closure of TransAlta's coal facility ahead of agreed upon dates regardless of this or any other regulation. While a positive development, without determining whether this closure resulted from Clean Air Rule incentives, as discussed in the about section additionality, these facilities should not be credited with ERUs as voluntary participants.

G. Electricity Sector Exemption for CPP Compliance

In response to feedback from utilities on conflicts between the Clean Air Rule and the federal Clean Power Plan (CPP), the Department chose to exempt electricity from Clean Air Rule compliance once an EPA-approved plan begins to cover the sector (WAC 173-442-040 (4)). While we would have preferred a rule that could have been used as a state-measures plan under the CPP, given the decision to pursue an incompatible baseline-and-credit architecture and Clean Air Act limitations on out-of-state generation, this exemption may help resolve some of the layered compliance issues.

Given this exemption, however, it would be unacceptable to use the federal CPP to loosen restrictions on Washington's utility sector. While the draft says that the final plan submitted to the EPA must have more stringent requirements than found in federal rulemaking, we urge the Clean Air Rule to specify that any CPP plan must be at least as ambitious as the requirements for other in-state sectors covered under the Clean Air Rule. More importantly, a compliance pathway for the Clean Power Plan should not be limited to the current Clean Air Rule reduction of 1.7 percent/year and rather be based upon stronger science-based targets for emissions reduction.

H. Biofuels

The proposed rule does not include biofuels under the list of exempted sources of GHG emissions. Achieving maximum GHG emission reductions in Washington state will require using a range of abatement tools, including cleaner transportation fuels. While best practice would require employing a life-cycle analysis of fuels covered by the rule, we understand that this is not an option in the current legal framework. Treating biofuel emissions the same as fossil fuel emissions, however, is not accurate and misses a key opportunity to support a low carbon solution.

We recommend that biofuels be treated as they are in [California's](#) cap-and-trade program, which exempts carbon dioxide emissions from biomass from both facilities and mobile sources from the GHG market. This would ensure that biomass used for fuels is treated consistently with biomass for industrial sources. Ultimately, lifting both of these restrictions in state law and allowing a more comprehensive analysis of their carbon attributes is the superior approach.

I. Additional Recommendations

Immediate inclusion of EITE facilities

We strongly support accommodations for energy intensive and trade exposed businesses to ensure that they continue thriving in Washington state. In particular, assigning to these businesses an output-based baseline provides flexibility for business growth and expansion that remains consistent with the

imperative to reduce carbon emissions, while also reducing the incentive to shift production to other jurisdictions. We recommend, however, eliminating the three-year compliance exemption for these facilities, which merely serves to delay urgently needed pollution reduction.

Prevention of adverse impacts

Ecology should consider the impacts of its draft design concepts on local air quality across Washington, particularly in communities that are already adversely impacted by air pollution. Depending on how an entity chooses to meet the cap, its use of credits might result in increased emissions of harmful air and water co-pollutants. To avoid this outcome, we recommend that the Rule require monitoring its impact on local air quality, particularly around existing pollution hot spots, to ensure that it does not create or exacerbate pollution hot spots and result in back-sliding on air and water quality.

CONCLUSION

As always, we remain committed proponents of state action to tackle climate change and reduce carbon pollution. We commend the work of the Department of Ecology and Governor Inslee in pursuing this regulation. Done right, the Clean Air Rule has the potential to make a significant contribution to carbon pollution reduction in Washington and set a national example for climate action. We acknowledge the improvements from the previous draft rule, and we urge you to consider the suggested changes offered above, and those provided by our partners at SEI, to craft the strongest possible rule.

We recognize that the Clean Air Rule relies on limited authority and cannot be the comprehensive carbon reduction package Washington needs and we all want. Regardless of the final form of the Clean Air Rule, we remain committed to continued partnership with you to draft policy through both regulation and legislation. In partnership, we can realize the benefits of the clean energy transition for Washington and all of its residents.

As you consider changes to the Clean Air Rule over the coming weeks, we stand ready to lend our expertise and counsel. Thank you for your hard work.

Sincerely,



Vlad Gutman
Climate Solutions



Bill Arthur
Sierra Club



Noah Long
Natural Resources Defense Council



Jamesine Rogers Gibson
Union of Concerned Scientists



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